# LEGISLATIVE SERVICES AGENCY
## OFFICE OF FISCAL AND MANAGEMENT ANALYSIS
200 W. Washington, Suite 301
Indianapolis, IN 46204
(317) 233-0696
http://www.in.gov/legislative

## FISCAL IMPACT STATEMENT

**LS 7335**
**BILL NUMBER:** HB 1598

**NOTE PREPARED:** Apr 15, 2009
**BILL AMENDED:** Apr 9, 2009

**SUBJECT:** Logistics Development Incentives.

**FIRST AUTHOR:** Rep. Reske
**FIRST SPONSOR:** Sen. Charbonneau

**BILL STATUS:** As Passed Senate

**FUNDS AFFECTED:** X **GENERAL**
X **DEDICATED**
**FEDERAL**

**IMPACT:** State & Local

**Summary of Legislation:** *County Wheel Tax:* This bill authorizes a county to adopt an ordinance providing a temporary exemption from the wheel tax for vehicles owned and used in the operation of twenty-first century logistics enterprises at certain locations.

*CVET:* The bill authorizes a county to adopt an ordinance providing a temporary exemption from the Commercial Vehicle Excise Tax (CVET) for vehicles owned and used in the operation of twenty-first century logistics enterprises at certain locations.

The bill limits the exemptions to vehicles owned and used at a new logistics enterprise or in the expansion of the fleet of an existing logistics enterprise. It also requires the Indiana Economic Development Corporation (IEDC) to certify the owner's eligibility for an exemption.

*Patents:* This bill modifies the adjusted gross income tax exclusion for certain income derived from the exploitation of certain patents by defining "development process", by allowing a clinical trial that is part of a development process, if any, to take place outside Indiana, and by providing that receipts attributable to the sale of a qualified patent also include the fair market value of receipts allocable to a qualified patent as the result of the sale of a trade or business.

**Effective Date:** July 1, 2009; January 1, 2010.

**Explanation of State Expenditures:** *CVET and County Wheel Tax:* The IEDC would have additional duties under this bill to verify that a vehicle owner is eligible to receive the exemptions and to issue certificates of eligibility. The IEDC should be able to complete these tasks with their current level of resources.

The Bureau of Motor Vehicles (BMV) would incur minimal administrative costs related to exemption of certain vehicles from the Wheel Tax and CVET (for intrastate vehicles). The fund affected is the Motor Vehicle Highway Account, which supports the BMV.

In addition, the Department of State Revenue (DOR) administers CVET as it relates to interstate vehicles and would also incur minimal administrative costs related to exemption of certain vehicles from CVET. The DOR is funded from the state General Fund.

*Patents:* Department of State Revenue (DOR): The DOR will incur additional expenses to revise tax forms, instructions, and computer programs to reflect this bill's various changes to the qualified patent income tax exemption. The DOR's current level of resources should be sufficient to implement the changes.

**Explanation of State Revenues:** (Revised) *Patents*: This bill makes several changes to the qualified patent income tax exemption, and the changes are effective beginning in tax year 2010. The potential fiscal impact resulting from the bill's changes to the exemption is indeterminable. The qualified patent income tax exemption passed in 2007, and so data is unavailable for the current impact because it will be reported on 2008 tax returns.

The bill changes the total amount of exemptions for patent-derived income that a taxpayer may claim in a taxable year from $5 M to $500,000. The bill exempts royalties, milestone payments, and receipts attributable to the sale of a qualified patent, including the fair market value of receipts allocable to a qualified patent as the result of the sale of a trade or business. Current statute exempts licensing fees, royalties received for the infringement of a qualified patent, receipts from the sale of a qualified patent, or other income received for the use of a qualified patent. The bill also includes the discovery and conception of the underlying invention and the reduction of the underlying invention to practice in the definition of "development process". The patent tax exemption is for inventions resulting from a development process conducted in Indiana.

*Background Information on the Patent Exemption* - A taxpayer may claim the exemption for 10 years with respect to a particular patent. The total amount of exemptions for patent-derived income that a taxpayer may claim in a taxable year is $5 M under current law. The current maximum exemption translates into a $170,000 reduction in tax liability for an individual taxpayer and a $425,000 reduction in tax liability for a corporate taxpayer or financial institution. Thus, if 10 taxpayers qualify for the maximum exemption amount each year, the annual revenue loss could range from $1.7 M (if all the taxpayers are individuals) to $4.25 M (if all the taxpayers are corporations) under current law. The new maximum exemption translates into a $17,000 reduction in tax liability for an individual taxpayer and a $42,500 reduction in tax liability for a corporate taxpayer or financial institution. Therefore for the same 10 taxpayers, the revenue loss would range from $170,000 to $425,000 respectively.

Since 1998, an average of about 1,560 patents of all types (utility, plant, design, and other patents) have been granted annually to individuals or entities in Indiana. However, annual patent totals for Indiana have declined in recent years from a high of 1,745 in 2002 to a low of 1,385 in 2007. The annual patent total is attributable primarily to utility patents, with utility patents granted averaging about 1,300 per year, or 84% of total patents since 1998.The annual total for utility patents granted to Indiana persons or entities also has declined from a high of 1,439 in 1999 to 1,137 in 2007.Data is unavailable for the number of plant patents granted and the income generated by patents granted to individuals or entities in Indiana.

Definitions: (1) A design patent may be granted to anyone who invents a new, original, and ornamental design for an article of manufacture.

(2) A plant patent may be granted to anyone who invents or discovers and asexually reproduces any distinct and new variety of plant.

(3) A utility patent may be granted to anyone who invents or discovers any new, useful, and nonobvious process, machine, article of manufacture, or composition of matter, or any new and useful improvement thereof.

**<u>Explanation of Local Expenditures:</u>**

**<u>Explanation of Local Revenues:</u>** (Revised) *CVET and County Wheel Tax:* Under this proposal, certain motor vehicles owned by a twenty-first century logistics enterprise could be temporarily exempted by the county fiscal body from the county wheel tax and the CVET if the enterprise is located in a qualified location. Qualified locations under the bill would include all brownfields, and also sites that are no more than three miles from an airport, a port, a freight railroad depot, a commuter rail station, a rail yard, a classification yard, an intermodal port, or an interstate highway.

The county fiscal body would have to pass an ordinance between July 1, 2009, and October 30, 2009, inclusive, for exemptions in 2010, 2011, 2012, 2013, and 2014. The exemption would be available only for vehicles that are either (1) used at a qualifying enterprise that begins operations at the location after December 31, 2009, or (2) purchased as part of a fleet expansion by an existing qualifying enterprise.

*County Wheel Tax:* In CY 2007, 44 counties imposed the Surtax/Wheel Tax and generated $5.8 M in Wheel Tax (and $51.5 M in Surtax). Wheel tax rates range from $5.00 to $40.00 per vehicle. Wheel Tax is distributed to the county unit and each city and town in the adopting county. The revenue is used for road and street construction and maintenance.

Currently, if additional commercial vehicles are registered in a county that imposes the Wheel Tax, then the additional commercial registrations would generate additional wheel tax. If the new qualified vehicles are exempt for five years under this bill, then the additional wheel tax would be foregone for those exemption years.

*CVET:* Under current law, each taxing unit's CVET distribution is equal to 105% of the amount that the unit received in the prior year, going back to the base year. The CVET tax rate is calculated by dividing the amount needed to make the unit distributions by the commercial vehicle registration fees paid in the previous year. The rate is applied to current registrations to generate the current year CVET liability for each vehicle.

Currently, if additional commercial vehicles are registered and the total of all commercial registration fees increases, the CVET tax rate is reduced, yielding the same total CVET distribution to local taxing units. If the new qualified vehicles are exempt for two or three years under this bill, the CVET rate would not be reduced in those years and the distributions to local units would be unaffected.

The exemptions from the Wheel Tax and CVET would be a local decision.

*Patents:* Because the changes to the patent income tax exemption in this bill may serve to decrease taxable income, counties imposing local option income taxes may experience a decrease in revenue as a result.

**State Agencies Affected:** IEDC; BMV; DOR.

**Local Agencies Affected:** Counties, cities, and towns; Counties with local option income taxes.

**Information Sources:** U.S. Patent and Trademark Office, Patent Counts by Country/State and Year, January 1, 1977-December 31, 2007.

**Fiscal Analyst:** Bob Sigalow, 317-232-9859; Jessica Harmon, 317-232-9854.